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In the

Supreme Court of the United States

FEBRUARY TERM 1967

NATIONAL SURETY CORPORATION,

Petitioner,

v.

RAUSCHER, PIERCE & CO., INC.,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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I.

The National Surety Corporation, your petitioner, prays that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the Fifth Circuit entered in the above entitled case on December 13, 1966.

II.

The opinion of the Court of Appeals for the Fifth Circuit is reported at 369 F. 2d 572. It is attached as Appendix A. infra, pages A-1 through A-14. The findings and conclusions of the trial court are attached as Appendix B, infra,

pages B-1 through B-10. The date of the decree sought to be reversed is December 13, 1966, and the time of its entry was December 13, 1966. A motion for rehearing duly filed was overruled on February 13, 1967.

III.

The jurisdiction of the District Court was invoked under 28 U.S. Code, §1332. This court's jurisdiction is invoked under 28 U.S.C.A. §1254, on the grounds that:

(1) The Court of Appeals affirmed the judgment of the lower court on findings of fact and conclusions of law rejected by the lower court as grounds for recovery, and thereby so far departed from the accepted and usual course of judicial proceedings as to call for this Court's power of supervision;

(2) The Court of Appeals affirmed the judgment of the trial court on new findings which included a finding that Rauscher, Pierce was itself defrauded, which finding is not supported by any evidence, wherefore the judgment rendered is without due process of law and so far departs from the usual accepted course of judicial proceedings as to call for this court's power of supervision; and

(3) If the Court of Appeals was correct in integrating the several steps in the transaction so as to make one transaction of the purchase by Rauscher, Pierce from the Underwriter for the Water District and the sale by Rauscher, Pierce to Water Bond Purchasers, then in

refusing to offset the damages sustained in the settlement with Water Bond Purchasers by the profit realized from the sale to Water Bond Purchasers, the court has decided an important question in conflict with applicable state law requiring the exercise of this court's power of supervision.

GENERAL STATEMENT

Because the facts concerning the issues here made are not disclosed in the opinion of the Court of Appeals, this statement is deemed necessary:

This suit was instituted by respondent, Rauscher, Pierce and Company, Inc., herein called Rauscher, Pierce, against petitioner, National Surety Corporation, herein called National Surety, on a Brokers Blanket Bond, conditioned to indemnify Rauscher, Pierce from:

> "(A) Any loss through any dishonest, fraudulent or criminal act of any of the Employees, committed anywhere and whether committed alone or in collusion with others, including loss of Property through any such act of any of the Employees."

The Bond contained a provision that:

> "The Underwriter will indemnify the Insured against court costs and reasonable attorneys' fees incurred and paid by the Insured in defending any suit or legal proceeding brought against the Insured to enforce the Insured's liability or alleged liability on account of any loss, claim or damage which, if established against the Insured, would constitute a valid and collectible loss sustained by the Insured under the terms of this bond * * *" (Tr. 330-331) (Ex. 3)

The loss claimed was amounts paid by Rauscher, Pierce in defense and settlement of two certain suits brought by Connecticut Mutual Life Insurance Company and State Mutual Life Assurance Company of America, herein called Water Bond Purchasers (as in the opinion of the Court of Appeals), to rescind a sale by Rauscher, Pierce to said Water Bond Purchasers of $1,365,000.00 of Travis County, Texas, Water Control and Improvement District No. 9 Bonds, which were alleged to have been purchased by Water Bond Purchasers because of misrepresentations of facts by one Volz, an employee of Rauscher, Pierce, and on which sales Rauscher, Pierce realized a net profit of $59,436.55. (R. 159)

When the suits were instituted against Rauscher, Pierce, it tendered the defense thereof to National Surety, which refused to defend on the ground that the recovery sought by the suits would not have been a loss within the coverage of its bond. Tr. 335) Rauscher, Pierce then employed attorneys and expended $32,331.07 for attorneys' fees and court costs, and settled the cases under an agreement to repurchase the bonds over a period of years at 75% of their face value (Exhibits 75 and 76), with resulting loss dependent on the value of the bond at the time of each respective purchase.

The issues here involved arose by reason of the complete about-face evidenced by the allegation of paragraph 7 of the original complaint of Rauscher, Pierce and paragraph 7 of its amended complaint.

Paragraph 7 of the Original Complaint (filed September 19, 1963), consisted of this short, unequivocal averment of facts:

> "7. The bonds, referred to in paragraphs 5 and 6 above, were sold to the stated purchasers by plaintiff for its own account, *the plaintiff having purchased such bonds previously from the Underwriter for the District.*" (Emphasis ours).

By First Amended Petition (R. 224), Rauscher, Pierce for the first time contended in an amended paragraph 7, (R. 228-229), that it purchased from the Underwriter "only after having commitments from the Connecticut Mutual and State Mutual to purchase the said bonds from it" * * * whereby any representation by Volz to Connecticut Mutual or State Mutual "was thus a representation to plaintiff as well." (R. 228-229). This was expanded in said amended complaint (R. 259-260) to include the additional allegation "that plaintiff's original commitment to purchase said bonds and its later purchase of them was decided upon by it in reliance on the same information and representations by Volz that he made to Connecticut Mutual and State Mutual. Any misrepresentation by Volz to Connecticut Mutual or to State Mutual * * * was accordingly a misrepresentation to plaintiff." (R. 259, 260).

The case was tried to the court without a jury. The trial court by its findings of fact and conclusions of law (Tr. 345-353) bottomed its judgment on the theory that the complaint of Water Bond Purchasers against Rauscher, Pierce stated a claim which if proved would have constituted a liability under petitioner's bond, and that petitioner's refusal to

defend rendered it liable for attorneys' fees and the amount paid by petitioner in settlement. (R. 345) No account was taken of the $59,436.55 net profit which Rauscher, Pierce realized on the sale to Water Bond Purchasers.

This judgment was affirmed by the Court of Appeals; but, as petitioner conceives, upon a theory different from that adopted by the trial court in its findings and conclusions, to-wit, on the theory advanced by respondent's amended complaint which was rejected by the trial court as grounds of recovery, and which is without evidence to support it.

IV.

STATEMENT AND ARGUMENT UNDER III (1)

The Court of Appeals affirmed the judgment of the trial court on a theory rejected by the trial court as grounds for recovery.

The judgment of the Court of Appeals rests on the ground that Rauscher, Pierce purchased the Water District Bonds simultaneously with the sale by it to its customers, and that the purchase by Rauscher, Pierce was induced by the same alleged fraudulent representations made by Volz to the customers of Rauscher, Pierce. This was a theory presented by Respondent in its amended complaint, directly contrary to its allegations in the original complaint that the plaintiff "purchased such bonds previously from the underwriter for the District" * * * (Paragraph 7, Original Complaint, R. 212)

The judgment of the trial court is based upon the following specific findings and conclusions of law:

"The plaintiff states it in words like this:

"The complaints of Connecticut Mutual Life Insurance Company and State Mutual Life Assurance Com-

pany of America sought to enforce an alleged liability which, if proved, would constitute a loss covered by 'Fidelity' provision A of the bonds.

"These allegations obligated this defendant to defend those suits under the provisions of the bonds conditioned to indemnify against attorney's fees and court costs of any proceeding to enforce insured's liability on account of any loss which, if established, would constitute a collectible loss under the bond." (R. 345).

The determinative conclusions of law were:

"The rescission suits brought against the plaintiff involved $1,500,000.00 and alleged and claimed the bonds were bought under fraudulent misrepresentations made by plaintiff's agents and representatives.

"When defendant was called upon to defend such suits under the terms of the bond or indemnity contract, it refused to do so upon the grounds that the suits in question did not come within the provisions of the indemnity agreement.

"By refusing to defend the suits, the defendant became bound to pay to the plaintiff the cost of procuring counsel to defend such suits and the costs of the court as set forth in the findings of fact, or to hold itself ready to pay whatever losses the plaintiff might sustain by reason of any judgment entered in such litigation." (R. 351).

These findings and conclusions constitute negative findings and conclusions on all of the facts upon which petitioner finally relied in the Court of Appeals and upon which the judgment of the Court of Appeals is based.

There is in the findings of the trial court this statement:

"The plaintiff, Rauscher, Pierce and Company, had a long-time employee, one Volz, who investigated matters and helped in making purchases and sales of bonds.

> He appears to have had the absolute confidence of his employers for a number of years. He is now dead. He was furnished by Tucker a report of the engineer and a lot of data touching the makeup of the Water District, of its assets and probable financial ability to meet its obligations. Volz wrote letters and furnished the engineer's report that had been made up for Tucker or under his supervision and that of the District, and it was upon this information and the information received by Volz in examining the property, the acreage, number of inhabitants, etc., that the purchase was made."

This is a mere random statement not tied to any ultimate findings of fact or any conclusions of law upon which the judgment is based. It constitutes a mere straw in the wind; but upon it Respondent was forced to tie its whole case, both findings of fact and conclusions of law and upon it the judgment of affirmance by the Court of Appeals must necessarily be based. Therefore, the Court of Appeals has in effect held that there was embodied within this random statement these findings:

(A) Rauscher, Pierce purchased the bonds from the underwriters only after commitment from Bond Purchasers and solely in reliance upon misrepresentations made by Volz in his letter to Water Bond Purchasers, whereby Volz perpetrated a fraud on Rauscher, Pierce.

(B) The misrepresentations made by Volz to Bond Purchasers were thus misrepresentations by Volz to Rauscher, Pierce whereby Rauscher, Pierce was induced to purchase the bonds from the District by reason of the fraud perpetrated upon it by Volz.

Clearly there was no such findings by the trial court. And since the trial court was urged to so find but did not, but to the contrary based its finding on the allegation and theory of liability of the original complaint, the function of the Court of Appeals on Respondent's abandonment of the theory of recovery upon which judgment of the trial court was based was to reverse and remand with direction to render judgment for petitioner. In ignoring the theory of recovery of the trial court, and affirming on independent findings and conclusions of its own, the Court of Appeals has set aside the findings of fact and conclusions of law of the Trial Court and rendered judgment on findings of its own having no basis in the evidence. The Court has therefore so far departed from accepted rules of law as to call for the exercise of this court's power of supervision.

Rule 52 with reference to findings by the court and the effect thereof is as follows:

> "Rule 52. Findings by the court. (a) Effect. In all actions tried upon the facts without a jury or with an advisory jury, the court shall find the facts specially and state separately its conclusions of law thereon, and judgment shall be rendered pursuant to Rule 58; . . ."

Therefore, whether fraud was committed on Rauscher, Pierce was a fact for determination of the trial court. *Massey-Ferguson, Inc. v. Bent Equipment Company*; 283 F. 2d 12, 15, (5th Cir. 1960). It was not the function of the Court of Appeals to make this finding. *Southland Corporation v. Campbell*, 358 F. 2d 333. (5th Circuit 1966)

In the case of *Southland Corporation v. Campbell*, 358 F. 2d 333 (5th Circuit 1966), the principal issue in the case

was one of purpose of Murchison Brothers acquisition of control of a corporation. Whether the principal purpose was evasion of income tax was not considered by the trial court, and in passing upon this the Court of Appeals said:

> "The issue of 'principal purpose' is one of fact. For us to hold that the 'principal purpose' of this acquisition of control was 'evasion or avoidance of Federal income tax', when the court below failed to consider this matter, and when the facts suggest a contrary conclusion, would be wholly inappropriate."

In *Randall Foundation v. Riddell*, 244 F. 2d 803 (9th Circuit 1957), the Court of Appeals of the 9th Circuit refused to make findings on stipulations in the record for reasons shown in this brief comment:

> "Appellant urges that, since there is a written stipulation as to certain facts, this Court must disregard the findings of the trial court and decide the case on our interpretation of the documents. Some courts have presumed to state such a rule where the evidentiary facts are entirely based upon stipulation or documents. Even there, an unwarranted circumscription of the powers of the trial judge is involved. Furthermore, the appellate court would assume thereby the power of making findings of fact, which passed out of the federal system with the abolition of trials do novo. The appellate courts of the federal system have such power neither inherently nor by grant, express or implied."

Again the 9th Circuit, in *Deering-Milliken & Co. v. Modern-Aire of Hollywood*, 231 F. 2d 623, (9th Circuit 1956) said:

> "There was considerable evidence in the record from which there is a possibility a contract, partially in writ-

ing and partially oral, might be spelled out. But this would require findings of fact as to intention, consideration, and definiteness. It is not within the competence of this Court to make such findings even if it were possible upon the record here, a point upon which no opinion is expressed."

STATEMENT AND ARGUMENT UNDER III (2)

There was no evidence to support the findings upon which the judgment of the Court of Appeals is based and therefore that judgment was rendered without due process of law.

As noted under III (1), supra, the judgment of the Court of Appeals rests upon findings that Rauscher, Pierce purchased the bonds only after commitment from bond purchasers and solely in reliance upon representations made by Volz in his letter to bond purchasers.

1. The finding that Rauscher, Pierce purchased the bonds only after commitment from Bond Purchasers is not supported by evidence.

The written agreement between Rauscher, Pierce, acting by its Vice President, Kocurek, and the Underwriter, James E. Tucker & Co., is dated January 31, 1961 (Ex. 25), and is in pertinent part as follows:

> "This letter will confirm agreement whereby *we have purchased* from you the above issue of bonds at the price of 96¼ and accrued interest. Our understanding is that these bonds come to us free of all charges with the exception of the legal opinion of McCall, Parkhurst & Crowe, the cost of which will be borne by us." (Emphasis ours).

This agreement was so understood by the Underwriter, who on the same day replied by its representative R. E. Whitlock as follows: (Ex. 26).

> "I am enclosing confirmation of sale to you of $1,500,000 Travis County Water Control & Improvement District No. 9 bonds at 96.25 plus accrued interest.

Accompanying this letter was a schedule of the bonds. (Ex. 27).

On January 31, 1957 Kocurek wrote to Russ and Company as follows. (Ex. D-9).

> "Re: $1,500,000 TRAVIS COUNTY W.C. & I.D. #9, 4½%, 4¾%, 5%, Unlimited Tax and Revenue Bonds:
>
> "This will confirm agreement whereby the above bonds are being put into a selling account at the price of 98 and accrued interest, with the understanding that your firm is taking a $250,000 participation.
>
> "As agreed, we will make offerings of these bonds for the benefit of the joint account to out-of-state institutions, we to be allowed a one point takedown on any sales that may be made. It is contemplated that no general offering will be made for approximately two weeks.
>
> "We also may invite another firm to join this selling group on the same basis agreed upon with you.
>
> "We are pleased to have you associated with us in this deal as we feel sure that it will be profitable for all."

On February 4, 1957 an almost identical letter was written by Kocurek to Columbia Securities Corporation. (Ex. D-10).

In connection with the letter to Russ and Company, Kocurek was asked:

> "Isn't it a fact that when you made your deal to close it on January 31st with Whitlock, that you considered those bonds belonging to Rauscher, Pierce.
>
> "A. Provided they are regularly issued." (R. 171).

Kocurek testified by deposition in the suits by the Water Bond Purchasers, and on cross-examination in this case did not deny, that he testified in those cases that Rauscher, Pierce owned the bonds at the time it wrote the letters to Russ and Company and Columbia Securities Corporation (R. 171); nor did he deny that in answer to questions as to whether Rauscher, Pierce owned the bonds at the time of offering them to Connecticut Mutual he made these statements:

> "Sure, we didn't offer the bonds until after we owned them ourselves." * * *
>
> "I know we would not have put prices on the bonds that we did not even own, or didn't have coupon rates on." (R. 173).

In Volz's letter to Connecticut Mutual dated February 2, 1957, it was stated, "We own and will offer to you * * * an issue of $1,500,000 Travis County, Texas Water Control and Improvement District No. 9 * * * bonds." (Ex. 6).

The opening statement of the Rauscher, Pierce circular accompanying this letter is, "We own and offer" $1,500,000 * * * bonds, etc." (Ex. 7).

Connecticut Mutual's confirmations were by letters of February 12, 1957 (Ex. 9), and March 4, 1957 (Ex. 12). (See also Exhibits 10 and 11).

There is thus no factual basis for the claim that Rauscher, Pierce purchased from Tucker after the confirmations by Water Bond Purchasers of their purchase from Rauscher, Pierce; and hence the purchase of Rauscher, Pierce could not have resulted from anything contained in the letters to Water Bond Purchasers.

Rauscher, Pierce well knew the representations contained in the engineers report before Volz wrote his letters to Water Bond Purchasers. Upon the first trip of Volz to look at No. 9, he brought with him an engineering report; Mr. Kocurek looked at it and said: "if this is half as good as the engineering report says, the bonds will be very good." Thus the representations of Volz, which merely repeated the facts stated in the engineering report, could not have been a representation to Rauscher, Pierce, since it already had these representations in the engineering report.

2. Volz made no representations of fact to Rauscer, Pierce and hence there is no evidence to support the finding of the Court of Appeals that Volz perpetrated a fraud on Rauscher, Pierce.

As respects the acquisition of the bonds, Kocurek testified (R. 138) that Rauscher, Pierce had been interested in several Travis County Water Improvement District Bonds prior to No. 9, to-wit, 5, 6, 7 and 8. Mr. Volz evaluated them and made recommendations; and Rauscher, Pierce did not get into trouble on any of them. (R. 139). In the early part of 1957 Kocurek learned of District No. 9, and that Tucker was interested in it. Tucker was contacted and an attempt made

to work out a joint account with him. (R. 140). Kocurek asked Volz to inspect the District and talk to Ted Whitlock, Tucker's representative. (R. 141). On cross-examination, Kocurek went into more detail with respect to the acquisition of the bonds. On No. 8, for instance, Volz didn't like it, then Kocurek went over and both of them looked at it together. Several people in Rauscher, Pierce's office were consulted. (R. 166). When Volz came back after looking at No. 9, he brought with him an engineering report. Kocurek looked at it and said, "If this is half as good as the engineering report says, the bonds will be very good." (R. 166-167). Finally Volz, Kocurek, Halpen and Kocurek's brother got together and discussed the situation. It was a joint decision.

Volz was not an engineer, and Kocurek admitted that it was not his business to check engineering data.

> "Q. You knew he didn't purport to check the engineering data, didn't you?
>
> "A. That is correct."

Volz made no representation concerning the engineering report. (R. 168).

> "Q. So what you were relying on from Mr. Volz was his judgment about the matter, from his looking over the district, showing the proximity of it to the city, the possibility for growth; in other words, an educated judgment as to whether the district would probably be a success, is that it?
>
> "A. That is correct." (R. 168-169).

The plaintiff's entire case on the question of fraud is suc-

cinctly stated by Rauscher, Pierce's own chief witness and attorney, Mr. Carrington. (R-122, 123). His personal knowledge concededly did not go to whether Volz was guilty or not and he did not attempt to so testify. He did not attempt to conclude or make any contention that it had been concluded that Volz was guilty of actual fraud. If Rauscher, Pierce's own chief witness and attorney did not reach that conclusion, it is submitted that the Court of Appeals was not justified in reaching that conclusion. The Court of Appeals was under a misapprehension that there was evidence to establish that Volz furnished the false information. There is no such evidence. The evidence shows that the Cameron Engineering Company supplied the information to Tucker which later turned out to be false and that Volz at most copied that information without knowledge of its falsity.

Rauscher, Pierce knew what Volz said in the offering circular was what the engineering report disclosed. On Volz's return from his first visit to the District with the engineering report, he presented it to Kocurek, who commented favorably upon it. This was long before the offering circular was made up from the engineering report. Since the offering circular contained nothing that was not already represented to Rauscher, Pierce by the engineering report, it is obvious that a claim that the offering circular was a representation to Rauscher, Pierce is wholly without substance.

STATEMENT AND ARGUMENT UNDER III (3)

If the Court of Appeals should be held to be correct in integrating the transactions so as to make for a simultaneous purchase by Rauscher, Pierce from the Underwriter and sale to Water Bond Purchasers, then Judge Reeves was correct in his dissenting opinion in holding that respondent was obliged to deduct from the loss sustained by it on the transaction the net profit of $59,436.55 realized on the sale to Water Bond Purchasers.

The testimony of respondent's Senior Vice President and Director is correctly quoted by Judge Reeves in the dissenting opinion. The statement made is taken from respondent's own testimony adduced at its own instance to show that after deduction and payments of all commissions and expenses "Rauscher, Pierce made, in connection with the purchase of the bond issue from Tucker and sales to Connecticut Mutual and State Mutual, $59,436.55. This profit of $59,436.55 was retained by respondent under claim of right to the fruits of the fraud perpetrated by Volz, thereby making Petitioner's bond conditioned to indemnify against loss from fraud of its employee, a guaranty that Rauscher, Pierce may retain the fruit of fraud perpetrated by an employee on third parties.

This theory of recovery the Court of Appeals was put upon the grounds that respondent was entitled to its bargain. But this theory of recovery of profit as damages runs counter to the settled law of Texas.

The Texas rule is so well stated in the Annotations to 124 ALR 65, that we quote it here:

> "The Texas court formerly followed the minority or 'out of pocket' rule, George v. Hesse (1906) 100 Tex. 44, 93 S.W. 107, 8 LRA (NS) 804, 123 Am. St. Rep. 772, 15 Ann. Cas. 456. And see 20 Tex. Jur. 190.
>
> "Thus, in George v. Hesse, supra, the court stated: 'The difference of opinion grows out of a confusion as to the nature of the cause of action. This is not a case in which the plaintiff sues for a breach of a contract — for the contract has been performed by both parties. But it is a case in which the plaintiff sues to recover damages for fraudulent representation by which he has been induced to enter into a contract to his loss. Clearly we think the extent of his loss is the difference between the value of that which he has parted with and the value of that which he has received under the agreement.'
>
> "This doctrine was later abrogated in part by a statute which, after defiining actionable fraud with regard to 'transactions in real estate or in stock in corporations or joint stock companies,' provided that 'all persons guilty of such fraud shall be liable to the person defrauded for all actual damages suffered, the rule of damages being the difference between the value of the property as represented or as it would have been worth had the promise been fulfilled, and the actual value of the property in the condition it is delivered at the time of the contract'. Sibley v. Southland L. Ins. Co. (1931; Tex.) 36 S.W. 2d 145. And see 20 Tex. Jur. 190; 2 Tex. Jur. Supp. (1937) 1363, 1364.
>
> "It will be noted that, by its own terms, this statute applies only to transactions in real estate and in stock in corporations or joint stock companies. The Texas courts are continuing to apply the rule stated in George v. Hesse, supra, in transactions involving personal property other than stock.

In *Morriss-Buick Co. v. Pondrom*, 113 S.W. 2d 889 (1938) the Commission of Appeals in an opinion adopted by the Supreme Court said:

> "After all there is nothing mysterious about a proper measure of damages, except the mystifying cases on the subject. The end desired is actual compensation for the injury—not profit. The true measure in every case of this kind is that rule which gives to the complaining party the actual amount of his loss resulting directly and proximately from the fraud practiced upon him. The rule announced above would do this unquestionably. That followed by the trial court might result in recovery of fictitious values."

Rauscher, Pierce is taking an inconsistent position in this litigation when it claims the right to retain the profits made on the sale of the water bonds. Rauscher, Pierce contends on the one hand that it has a claim under its indemnity bond becaues of an alleged fraud on the part of Volz, and then on the other hand Rauscher, Pierce ratifies the fraud by demanding that it be allowed to retain the profit which it has made as a result of such alleged fraud. There is an element of public policy involved here which does not sanction the retention by an employer of the fruits of an alleged fraud committed by an employee against third parties. It is our position that the fruits of such alleged fraud belong to the victims thereof, namely, the water bond purchasers and should be applied to to the reduction of any indebtedness of Rauscher, Pierce to such purchasers. In other words, even if Rauscher, Pierce's claim is covered under indemnity bond, it is only entitled to be placed in status quo ante.

For the reasons stated above, the decision of the Court of Appeals in the instant case raises a question of general importance to the law which should be reviewed by this Court.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, Lloyd E. Elliott, a member of the bar of the Supreme Court of the United States, do hereby certify that I have on this ..... day of March, 1967, mailed by first class mail, 3 copies of the foregoing Petition for Certiorari to Paul Carrington, 1700 Mercantil Bank Bldg., Dallas, Texas, attorney for respondent, Rauscher, Pierce & Company, Inc.

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Dallas, Texas 75201.

APPENDIX A

In the

UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 21903

NATIONAL SURETY CORPORATION,

Appellant,

v.

RAUSCHER, PIERCE & CO., INC.,

Appellee.

Appeal from the United States District Court for the Northern District of Texas.

(December 13, 1966.)

Before RIVES, BROWN and MOORE,* Circuit Judges.

BROWN, Circuit Judge: This appeal involves the question of liability under a Brokers Blanket Bond purchased to indemnify the Insured against any loss sustained due to dishonest, fraudulent or criminal acts of its employees and for court cost and reasonable attorney's fees incurred by the Assured in defending suits arising from such acts. The District Court sitting without a jury allowed Rauscher, Pierce and Company, Inc., the Assured, recovery in the amount of $73,131.07 against National Surety Corporation,

*Of the Second Circuit, sitting by designation.

that National Surety fulfill its indemnity bond obligation to defend the suit. National Surety refused on the basis that the suit was not a claim which came within coverage of the bond. After the refusal by National Surety, Rauscher, Pierce engaged legal counsel and after extensive investigation, pretrial activity and negotiation, a compromise agreement was worked out with the Water Bond Purchasers.

The settlement took this form. The Water District was to reissue bonds containing terms, conditions and provisions more consistent with actual conditions of the district than those in the original bonds. The reissued bonds were to remain the property of the Water Bond Purchasers. Rauscher, Pierce agreed, however, to repurchase the reissued bonds within eleven years in ten installments at 75% of their face value even though the actual value at the time of purchase might be less. To the extent, therefore, that the market value of the reissued bonds was less than 75%, Rauscher, Pierce was certain to sustain a loss at these installment dates.

After the compromise Rauscher, Pierce instituted suit against National Surety to recover its costs and the damages sustained. The District Court found National Surety liable. The Court held that the loss was within the coverage of the Brokers Blanket Bond and "[b]y refusing to defend the suits, * * * [National Surety] came bound to pay to the plaintiff the cost of procuring counsel to defend such suits and the costs of the court * * *." Likewise, it became obligated "* * * to hold itself ready to pay whatever losses the plaintiff might sustain by reason of any judgment enter-

ed in such litigation." The Court allowed Rauscher, Pierce to recover $32,311.07 expended in defending the suits and $40,800 actual loss based on the repurchase of bonds on two of the agreed ten installments occurring in the interim. Also the Court found that National Surety was to reimburse Rauscher, Pierce for any future losses it might sustain due to the repurchase of the remaining installments.

National Surety urges two errors: (1) no liability exists on its part because the claim asserted by the Water Bond Purchasers did not come within the coverage of the indemnity bond, and (2) in the event it is found liable, there should be set off against National Surety's liability the profit of $59,436.55 which Rauscher, Pierce made on the sale of the bonds to the Water Bond Purchasers.

We first consider National Surety's contention that the suits by the Water Bond Purchasers did not come within the coverage of the bond. The alternatives for supporting this position are few. National Surety must show either (1) that the suits instituted by the Water Bond Purchasers did not grow out of alleged fraudulent acts committed by the employees of Rauscher, Pierce, the Assured, or (2) that no loss was in fact sustained by Rauscher, Pierce.

We easily dispose of the first. It is clear from the face of the complaints filed by the Water Bond Purchasers that the alleged misconduct was sufficient to bring the suit within coverage of the indemnity bonds.[3] Actually National Surety

[3] The complaint filed by one of them shows:

"5. In connection with the offering to and purchase by plaintiff of these bonds from defendant, defendant caused

(Footnote—continued)

does not deny that the demand of the Water Bond Purchasers was based on alleged misrepresentations by Volz acting in his official capacity as representative of Rauscher, Pierce. Rather, as near as we can discern it, National Surety contends that the claims were not within the coverage becuase Rauscher, Pierce was in a position to avoid the prosecution of the suits without actually sustaining any loss. In their suits the Water Bond Purchasers demanded a rescission of the sale. In exchange for the full purchase price paid for the bonds, they tendered a return of the bonds together

(Footnote—continued from preceding page)

to be delivered to plaintiff through the United States mails a letter from one Edward T. Volz, its then Manager, Institutional and Dealer Sales, dated February 2, 1957, with which were enclosed and transmitted a circular describing said bonds and their issuer and a letter report of Cameron Engineering Company on said bonds and district issuing them dated 18 January, 1957, signed by one Homer Trimble as a registered professional engineer; and in addition made and caused to be made various other representations of fact, oral and written, regarding said bonds prior to their purchase by plaintiff.

"7. The said Edward T. Volz was at that time and at all times material hereto an agent and employee of defendant. In forwarding the aforesaid matter to plaintiff through said mails he was acting within the scope of his authority as Manager, Institutional and Dealer Sales of defendant.

"* * *

"12. Each and every statement and representation referred to in paragraphs 5, 8, 9 and 10 above was made for the purpose of inducing plaintiff to purchase the bonds and plaintiff was entitled to rely upon each such statement and did so to its damage in making such purchase.

"* * *

"15. The representations and statements made by defendant and referred to in paragraphs 5, 8, 9 and 10 were each untrue. Each was a misrepresentation of a material fact, made by defendant in the mistaken belief that it was true and made with the intent that plaintiff should believe it and rely upon it in deciding whether or not to purchase the bonds. Plaintiff did believe and rely upon each such misrepresentation, and each was a material factor in its decision

(Footnote—continued)

with all interest received thereon to date.[4] For reasons it fully explained, Rauscher, Pierce rejected the offer to rescind as not being a prudent disposition of the claims. National Surety argues that by rejecting the offer to rescind, Rauscher, Pierce eliminated any possible liability under the indemnity bond. The reasoning runs this way. Since Rauscher, Pierce could have rescinded the sale, this would have

(Footnote—continued from preceding page)

to purchase the bonds. Plaintiff and defendant were mutually mistaken about the truth of each such representation and statement. Had plaintiff known the true state of facts as o any of these misrepresented matters it would not have purchased the bonds. * * *.

"16. Each statement and misrepresentation referred to in paragraphs 5, 8, 9 and 10 was made by defendant with reckless disregard of its truth or falsity and as to the omission of relevant material facts in connection therewith, with the intent that plaintiff should believe it and rely upon it in deciding whether or not to purchase the bonds. Plaintiff did believe and rely upon each such misrepresentation, and each was a material factor in its decision to purchase the bonds. Had plaintiff known the true state of facts and to any of these misrepresented matters it would not have purchased the bonds. * * *.

"17. Each statement and misrepresentation referred to in paragraphs 5, 8, 9 and 10 was made by defendant when said defendant knew or should in the exercise of reasonable care have known it to be false and misleading as therein stated, and with the intent that plaintiff should believe it and rely upon it in deciding whether or not to purchase the bonds. Plaintiff did believe and rely upon each such misrepresentation, and each was a material factor in its decision to purchase the bonds. Had plaintiff known the true state of facts as to any of these misrepresented matters it would not have purchased the bonds. * * *."

The complaint filed by the other purchaser was substantially the same.

[4] The complaint filed by Connecticut Mutual Life stated:

"18. Plaintiff has heretofore claimed against defendant rescission of the sale of these bonds to it and offered physical tender to defendant of said bonds together with all interest received thereon. * * *

"Plaintiff * * * has been, and is now ready, willing and able to pay over and deliver to defendant said bonds and all interest received thereon by it; and plaintiff hereby makes its continuing tender and offer to do so and to do such all other equity as may be appropriate."

The complaint filed by the other was similar.

restored the status to the position existing prior to making of the sale. Rauscher, Pierce would have had the bonds, it would have given up the proceeds received on the sale by returning the purchase price to the Water Bond Purchasers. Thus everyone would be where they were earlier, and no loss would have been sustained by anyone. Countering this argument Rauscher, Pierce made out several strong points. The first is that in early stages of the litigation, there was reasonable expectation that a meritorious defense of laches could be made out. Additionally, had the suit gone to trial, there was the great possibility that under F.R.Civ.P. 54(c) the trial Court might award damages to the Water Bond Purchasers rather than merely grant the rescission. *Travelers Ins. Co. v. Busy Elec. Co.*, 5 Cir., 1961, 294 F. 2d 139. National Surety responds by asserting that these contentions were relevant only had the suits proceeded to trial. Since trial was avoided by compromise, this means in effect that Rauscher, Pierce lost all coverage since by exercising the proffered (but rejected) rescission, all "loss" could have been avoided. But we think this argument is without merit. This puts the Assured in the position of choosing at its peril between taking the safe way out by returning to the pre-sale status or simply relinquishing its coverage under the indemnity bond by insisting in good faith on its right to defend the suit. After all, to accept without hesitation the proffered rescission would be to concede liability, to concede the total absence of a defense, either complete or partial. But with coverage denied and the demand for defense rejected, the standard was one of taking that action which a prudent

uninsured security dealer would have taken. That course might lead to defense to the bitter end or defense for awhile and compromise as the exigencies suggested. *United Services Auto Assn. v. Russom*, 5 Cir., 1957, 241 F. 2d 296, n.9 and related text. On the merits the investigation at least for a long time indicated that Rauscher, Pierce might be able to reduce the loss considerably if damages, not rescission, were awarded. What made rescission so unattractive—both to the Assured and ultimately to the Insurer, was the great drop in market value of the bonds (about 60) in 1961 in contrast to 1957. At any rate, Rauscher, Pierce invited National Surety to take over settlement negotiations and to pass on proposed alternative settlements. But this, too, was met with a refusal. The wisdom and the prudence of the settlement simply is not challenged.

National Surety urges that as the sale of the bonds was made by Rauscher, Pierce acting as principal to allow recovery for damages after rejecting rescission would be to allow the principal to recover the fruits of its own fraudulent acts. This, it claims, would be against public policy. Rauscher, Pierce does not deny that it made the sale acting as principal, but it makes the undeniable response that it was placed in this situation because of the fraudulent misrepresentations made by Volz. Although the transaction had three steps, the record bears out, and the Court impliedly found, that no commitment to purchase the bonds from Tucker was made by Rauscher, Pierce until it had a firm commitment for resale to the Water Bond Purchasers. The theory is, then, that the false information furnished by Volz was

a fraudulent misrepresentation to them as much as to the Water Bond Purchasers. Consequently, the argument runs, since Rauscher, Pierce relied on Volz throughout the transaction and its liability to the Water Bond Purchasers was brought about by no illegal acts of its own, public policy is not offended by allowing it to recover for damages it sustained as principal because of fraudulent acts of its agent. *Hendrix v. Employers Mut. Liability Ins. Co.*, E.D.S.C., 1951, 98 F.Supp. 84.

In assaying this, we think National Surety is wrong in asserting that this theory that the Assured was itself defrauded by Volz was not before the Court or passed on by it. First, the proof was directed pointedly this way. And it was quite ample. Next, it matters not that the amendment to Par. 7 of the Complaint was after the demand to defend the suits by the Water Bond Purchasers. National Surety overlooks a material fact. Although that might have a bearing on whether attorney fees were recoverable for defending that suit, the Assured's claim is not for defense alone. The bond indemnifies them from loss sustained by it (see note 1, *supra*). That loss might be a direct one, e.g., from theft, embezzlement, etc., or because of liability to third persons. Here it showed it sustained a loss because it, too, was defrauded by the agent.

Of course, as to the claims by the Water Bond Purchasers, these fit the literal terms of the coverage (see note 1, *supra*). The duty to defend, of course, is ordinarily fixed by the allegations of the damage complaint. *Green v. Aetna Ins. Co.*, 5 Cir., 1965, 349 F. 2d 919.

National Surety next asserts that if it is liable under any circumstances it should be liable only to the extent the damages exceed the profits Rauscher, Pierce made on the sale of the bonds to the Water Bond Purchasers. To this Rauscher, Pierce makes several responses including procedural ones we ignore.

Rather, we think we should face up to the merits of whether the "loss of the bargain" sustained by Rauscher, Pierce is a damage which should come within the coverage of the indemnity bond. A reading, cursory or close, of the language in the indemnity bond reveals no limitations on the type or amount of losses covered. All that is required is that such loss is due to the "* * * dishonest, fraudulent or criminal act of any of the employees, * * *."

At the outset we start with the Texas rule that doubts in construction of the bond must be resolved against the surety. *Fidelity and Deposit Co. v. Central State Bank*, Tex.Civ.App., 1928, 12 S.W. 2d 611, 613; *Massachusetts Bonding & Ins. Co. v. Texas Finance Corp.*, TexCiv.App., 1924, 258 S.W. 250, error dismissed; *First State Bank v. Metropolitan Casualty Ins. Co.*, Tex., 1935, 79 S.W. 2d 835.

But we see no doubt and no reason to import doubt. We look on this as do the businessmen to this contract. On the one hand is a stock broker who runs the risk that it assets will be lost, squandered, or dissipated through unfaithfulness of its servants. On the other, is a surety company desperately trying to interest such businesses to insure against losses by purchasing protection from it at a premium which

will—it hopes—assure it a profit. The businessman is in the business to make money—make profits. When he loses assets, he loses what profits, current or past, have produced. The loss is the loss of assets—generally money—not the origin of such money. The loss is as real in nature and amount as that sustained when a third party recovers judgment for a fraudulent or dishonest act of an employee.

This Court held as much in *Eagle Indemnity Co. v. Cherry*, 5 Cir., 1950, 182 F. 2d 298. In that case the indemnity bond was much like the present one. The indemnity bond insured against "* * * Any loss of money or other property * * * which the insured shall sustain * * * through * * * fraudulent or dishonest act or acts committed by any one or more of the employees * * *." There the president of the company using his position of trust secretly purchased steel and resold it pocketing the profits without the transaction ever going through the company. We allowed the recovery of the profits from the indemnity company.

We regard *Penn National Hardware Mutual v. General Finance Corp.*, 5 Cir., 1926, 16 F. 2d 36, pressed so heavily by National Surety, as clearly distinguishable. In *Penn National*, the assured was in the business of financing the sale of automobiles and the indemnity agreement was to indemnify the assured against any loss sustained due to default on the mortgages by the mortgagor. It was not to indemnify against losses due to fraudulent or dishonest acts of the employees. In this pre-*Erie* case we merely construed that contract in saying, "[t]he policy did not insure against

the loss of profits * * *." The nature and range of the risks, almost unlimited in scope and potential amount (subject to the bond ceiling of $500,000) make the contract here of quite a different nature. Nor are we able to see how National Surety can get any comfort from *In re: Schluter, Green & Co.*, 4 Cir., 1938, 93 F. 2d 810. It did not present our problem. And except to say that *Kramer v. Linz*, Tex. Civ.App., 1934, 73 S.W. 2d 648, is easily distinguishable, it deserves no further comment.

The faithless employee committed fraudulent acts. It involved the Assured in serious charges since, although morally innocent, it was nevertheless accountable to others for actions of its servants. To settle the claim it had, or will have, to give up much that it would have kept. These were losses.

The occurrence was covered. So, too, were the losses. It is that much worse off than it would have been had not the servant fraudulently misled it and the customer. That was the risk underwritten. It is the one to be reimbursed.

AFFIRMED.

RIVES, Circuit Judge, dissenting:

The majority points out that: "Although the transaction had three steps, the record bears out, and the Court impliedly found, that no commitment to purchase the bonds from Tucker was made by Rauscher, Pierce until it had a firm commitment for resale to the Water Bond Purchasers. The theory is, then, that the false information furnished by Volz was a fraudulent misrepresentation to them as much as to the Water Bond Purchasers."

Arnold J. Kocurek, Senior Vice President and Director of Rauscher, Pierce, testified:

> "Q. Under that calculation from your books can you also say what profit net, after all deductions and payment of commissions and expenses Rauscher, Pierce made in connection with the purchase of the bond issue from Tucker, and the sales to Connecticut Mutual and State Mutual?
>
> "A. The figure is $59,436.55. That is before overhead.
>
> "Q. Now, the net figure, not including overhead, was what per cent?
>
> "A. It was 4 per cent of the par value of the bonds."

It seems clear to me that the loss of Rauscher, Pierce under the bond should be computed from the transaction as one integrated whole. I therefore respectfully dissent from the judgment of affirmance.

APPENDIX B

Amended Findings of Fact and Conclusions of Law

(Number and Title Omitted) (Filed: July 9, 1964)

The Court, having heard and considered Plaintiff's Motion for Amendments to and Additions of Findings of Fact and Conclusions of Law, files the following Amended Findings of Fact and Conclusions of Law in lieu of the Findings of Fact and Conclusions of Law heretofore filed in this cause.

Findings of Fact

This is a suit growing out of the alleged loss in the sale of securities, the loss allegedly being protected by an indemnity bond upon which suit is brought.

The plaintiff states it in words like this:

The complaints of Connecticut Mutual Life Insurance Company and State Mutual Life Assurance Company of America sought to enforce an alleged liability which, if proved, would constitute a loss covered by the "Fidelity" provision A of the bonds.

These allegations obligated this defendant to defend those suits under the provisions of the bonds conditioned to indemnify against attorney's fees and court costs of any proceeding to enforce insured's liability on account of any loss which, if established, would constitute a collectible loss under the bond.

The plaintiff says that about the 8th of September, 1956, and again on September 8, 1959, and again on September 8,

1962, it was issued by the defendant for a valuable consideration paid policies of insurance known as defendant's "Brokers Blanket Bond," such being intended to indemnify the broker against loss under certain conditions in the conduct of his business. The bond or indemnity obligation contained the following:

> "Fidelity (A) Any loss through any dishonest, fraudulent or criminal act of any of the Employees, committed anywhere and whether committed alone or in collusion with others, including loss of Property through any such act of any of the Employees.
>
> "COURT COSTS AND ATTORNEYS' FEES
>
> "(Applicable to all Insuring Clauses now or hereafter forming part of this bond)
>
> "The Underwriter will indemnify the Insured against court costs and reasonable attorneys' fees incurred and paid by the Insured in defending any suit or legal proceeding brought against the Insured to enforce the Insured's liability or alleged liability on account of any loss, claim or damage which, if established against the Insured, would constitute a valid and collectible loss sustained by the Insured under the terms of this bond. . . ."

Arnold J. Kocurek, an executive vice-president of Rauscher, Pierce, maintains an office for the plaintiff, Rauscher, Pierce, in the City of San Antonio. It was out of this office that the transaction took place which has led to this controversy.

There was during 1956 organized in Travis County in the vicinity of the City of Austin a Water Control and Improvement District designated as No. 9, organized by

authority of the statutes of Texas, an election being held in which the landowners within the District participated.

After the District had been fully organized and legally created, it issued bonds in the amount of $1,500,000 to be used to construct a water system within the District. The District in the sale of tis bonds entered into negotiations with James C. Tucker and Company of Austin who agreed to buy the bonds when authorized.

The plaintiff, Rauscher, Pierce and Company, had a long-time employee, one Volz, who investigated matters and helped in making purchases and sales of bonds. He appears to have had the absolute confidence of his employers for a number of years. He is now dead. He was furnished by Tucker a report of the engineer and a lot of data touching the makeup of the Water District, of its assets and probable financial ability to meet its obligations. Volz wrote letters and furnished the engineer's report that had been made up for Tucker or under his supervision and that of the District, and it was upon this information and the information received by Volz in examining the property, the acreage, number of inhabitants, etc., that the purchase was made.

The bonds were issued by the District and acquired by the plaintiff from Tucker about March, 1957. After they were issued to Tucker they were immediately turned over to the plaintiff, Rauscher, Pierce.

Rauscher, Pierce concluded a sale of a portion of these bonds to the State Mutual Insurance Company about the

29th of May, 1957, and to the Connecticut Mutual by delivery and payment by Connecticut Mutual on August 5, 1957.

About February 1, 1961, these two insurance companies addressed themselves to the plaintiff demanding a rescission of the sale of such bonds and restitution in full, claiming misrepresentation made by plaintiff's salesman Volz, on which they allegedly acted. The said insurance companies wrote letters in February, 1961, demanding the rescission of the purchase of said bonds from Rauscher, Pierce.

In June, 1961, the Connecticut Mutual filed suit against Rauscher, Pierce in the United States District Court of the Western District at Austin. The complaint as filed sought rescission and restitution because of the material misrepresentations made by Volz to the Connecticut Mutual in disregard of their truth or falsity and as to the omission of relevant and material facts in connection therewith. The State Mutual also filed suit with substantially the same allegations.

The defendant National Surety Company declined to assume the defense of these suits and declined to obligate itself to bear any of the court costs or to pay any of the attorneys' fees or to supply counsel, denying liability under its insuring clause.

Counsel for plaintiff, with counsel engaged in view of the situation, went into the files and proceeded to take depositions. They found some papers in the file of Mr. Volz and obtained certain matters by taking depositions that led

counsel to believe and to advise the plaintiff that it was in jeopardy of judgment by reason of the suits that had been filed by Connecticut Mutual et al.

Upon advice of counsel so had, the suits were compromised, by the terms of which the District was to issue refunding bonds containing conditions and provisions more satisfactory than those in the original bonds, in that the plaintiff would agree to buy these refunding bonds at a price of 75 per cent of their value within eleven years, buying them in ten annual installments.

These refunding bonds remained the property of the two insurance companies, but the plaintiff, under the terms of the settlement, was to purchase the same in annual installments at 75 per cent of their face value, even though the market value might be at a less figure.

Plaintiff offered to the defendant an opportunity to determine whether or not the litigation against plaintiff by Connecticut Mutual and State Mutual ought to be compromised and settled and, if so, upon what terms. The defendant refused so to do. Both settlement agreements were reasonably and prudently entered into by plaintiff in the termination of the two law suits against it by Connecticut Mutual and State Mutual, and the terms of both such settlement agreements were reasonable and prudent.

Acting under the settlement agreements, on November 20, 1962, the plaintiff Rauscher, Pierce purchased the first of these ten installments of bonds from Connecticut Mutual

and State Mutual at the price of 75% of the face value of the refunding bonds, as stipulated in the settlement agreement.

A second installment of refunding bonds was purchased by plaintiff in accordance with the settlement agreements on March 2, 1964, for the stipulated price equal to 75% of their face value.

The Court finds that Rauscher, Pierce suffered a loss upon November 20, 1962 at the time of the purchase of the first installment of refunding bonds, of the difference between 75% of the face value of the bonds and 60% of the face value of the bonds, their market value at the time being in amount a loss of $20,400.00.

The Court finds that Rauscher, Pierce suffered a loss upon March 2, 1964, at the time of the purchase of the second installment of refunding bonds, of the difference between 75% of the face value of the bonds and 60% of the face value of the bonds, their market value at the time, being in amount a loss of $20,400.00.

In handling this litigation to defend the suits of Connecticut Mutual and State Mutual, the plaintiff paid $31,176.52 in attorneys' fees, which was a reasonable fee, and court costs in the further sum of $1,154.55.

Rauscher, Pierce has properly and timely complied with all requirements of the indemnity bonds involved in this suit concerned with notices, tenders, or proofs of loss to defendant on the claims allowed herein. Further, the de-

fendant, in communications to plaintiff, waived any other or more formal proofs of loss or demands with respect thereto than the plaintiff made to it.

Conclusions of Law

The plaintiff Rauscher, Pierce was a broker handling large sums of money in bonds and securities. For an agreed price the defendant contracted to indemnify the plaintiff against loss sustained within the terms of the indemnity bond executed for that purpose.

The rescission suits brought against the plaintiff involved $1,500,000.00 and alleged and claimed the bonds were bought under fraudulent misrepresentations made by plaintiff's agents and representatives.

When defendant was called upon to defend such suits under the terms of the bond or indemnity contract, it refused to do so upon the grounds that the suits in question did not come within the provisions of the indemnity agreement.

By refusing to defend the suits, the defendant became bound to pay to the plaintiff the cost of procuring counsel to defend such suits and the costs of the court as set forth in the findings of fact, or to hold itself ready to pay whatever losses the plaintiff might sustain by reason of any judgment entered in such litigation.

After the defendant refused to defend the suits or to furnish counsel, the plaintiff, in consultation with his own counsel, began to take depositions and testimony and, under

advice of such counsel, from the information obtained, he was advised to compromise the controversy, which was done.

The arrangement and settlement included an agreement that refunding bonds of the Water District would be issued in lieu of the bonds in controversy, and an agreement that Rauscher, Pierce obligated itself to offer to purchase in ten equal installments such refunding bonds at a price equal to 75% of the face value of such refunding bonds, even though the market value of such at the time of a particular installment might be below 75% of their face value.

The plaintiff made the purchase of the first installment of the refunding bonds at a loss which it proposes the Court to find to be $56,400.00, based on a fair market value of 35% of the face value. The second purchase of the refunding bonds in like quantity approximately one year later entailed a loss of only $20,400.00, based upon a fair market value of 60% of face value. The evidence as to the market value of the particular securities on the first purchase is not very satisfactory or convincing. The securities were new and were involved in litigation. No market quotations appeared or were shown to exist as in the case of larger institutions. They were simply worth what they would bring. The evidence shows that the Water District was in distress and that the first purchase was made under circumstances while in such distress.

In the absence of better evidence as to the value of the refunding bonds at the time of the purchase by plaintiff of

the first installment, we believe that the figure of 60% of face value which the evidence establishes to be the fair market value of the refunding bonds at the time of the purchase of the second installment to be the most reliable proof of fair market value of the refunding bonds at the time of the purchase of the first installment. The Court has accordingly used that market value in finding the loss sustained by plaintiff on both the purchase of the first installment of refunding bonds and the purchase of the second installment of refunding bonds one year later.

Upon the issue of declaratory judgment, the Court holds and determines that the possible market value of these refunding bonds is by reason of the very nature of the case quite uncertain. Austin is a growing city and the District includes a large area and there is a possibility of the bonds going higher and increasing in value. On the other hand, financial stress might cause the bonds to bring a lower price. The most that we find that the Court can accomplish here is to interpret the contract to reimburse the plaintiff in whatever loss may develop in the next installments. Whether the bonds have a market value equal to 75% of their face value may or may not be a fact at the time of the purchase of any additional installment.

We think there should be a declaratory judgment without prejudice to either party to have the amount of any loss judicially determined on the occasion of each of the remaining eight installment purchases. If the bonds will bring the obligated price, then there would be no liability. If they fall

short, then the defendant is liable for the shortage which must either be ascertained between the parties themselves or by hearing before this court or other competent jurisdiction.

7-9-1964

/s/ T. Whitfield Davidson

United States District Judge